

# **Burlington Retirement Committee**

## ***Meeting of the Committee Members***

### **Agenda**

March 25, 2014 5 – 7pm

Burlington Electric Department (First Floor Conference Room)

585 Pine Street, Burlington, Vermont 05401

Meeting began at 5:12pm

Mayor Weinberger, Councilor Knodell, Councilor Bushor, Bob Rusten, Joe Keenan, Jeffrey Wimette, Mike Flora, Brian Lowe, Jim Strouse (by phone), and Bob Hooper (by phone) present  
Councilor Mason, Councilor Paul, Eileen Blackwood arrived late  
Bill Rasch, John Federico, and Susan Leonard absent

5:00pm – 5:05 pm      **Approve Agenda**

Approved unanimously - Jeffrey Wimette motioned, Councilor Knodell second

5:00pm – 5:05pm      **Review and Approval of March 11, 2014 meeting minutes**

Approved unanimously - Councilor Bushor motioned, Jeffrey Wimette second

Jeffrey Wimette noted that VPIC's Chairman Steven Rauh stated in the last meeting that VPIC has a practice of moving money to underperforming managers, which he and others thought was notable.

Barry Bryant offered as an explanation that this practice was meant to account for expected reversion to the mean in terms of manager performance.

5:05pm – 5:10pm      **Public Comment**

5:10pm – 5:50pm      **Barry Bryant, Managing Director at Dahab Associates, Presentation on Asset Management**  
*All*

Barry Bryant provides a historical review of VPIC, which he described as a professional outfit with good people, reasonable fees, and disappointing returns to date.

- 2008, the first year in VPIC, was a bad year – 30.4 percent loss that put the fund at about the 98<sup>th</sup> percentile (100 percent is the worst). VPIC held this same portfolio allocation and had strong returns (4<sup>th</sup> and 8<sup>th</sup> percentile – with 1 percent being the best)
- In 2011, VPIC staff turned over completely (to the current leadership)
- 2013 return is about half the median return, putting the return in the 95<sup>th</sup> percentile
  - This is a problem because 2013 was one of the years to make up some of the funding deficit for Burlington
  - The theory is that the conservative approach insulates the portfolio from market downturns.
  - However, Barry believes PIMCO has modeled VPIC's 2013 allocation against market returns from 2008 – 2013 and found that the portfolio does *worse* in 2008
    - The implication is that VPIC's strategy leads to lower returns in good years and does not insulate – and in fact could worsen – the fund's performance during a downturn

- Of note, a standard allocation index fund would have outperformed VPIC in three of six years and over 4 and 6 year timelines

Barry recommends a simpler portfolio approach

- Equity, fixed income, and alternative asset classes (timber, real estate, and emerging market equity)

Barry also outlined four potential different approaches with respect to VPIC:

- Retain VPIC exclusively and wind down non-VPIC assets
- Invest exclusively in index-based portfolio
- Run significant portfolio (\$50-100m) alongside VPIC to achieve better concerns on a competitive basis
- Run significant portfolio supplemental to VPIC taking an aggressive risk posture to supplement return

Barry advises tasking BERS with analyzing the situation (asset allocation study) and coming to a recommendation about the best way forward of the four options he outlined (p. 10 of his accompanying documents).

Councilor Bushor: Can you speak to the differences between the VPIC and BERS Board? Specifically, are there requirements at the state level for certain expertise? Could the BERS Board do the same job as VPIC?

Barry Bryant: BERS has just as much education and ability as VPIC, but has not been as focused. It could be as focused.

Jeffrey Wimette: You had mentioned at one point that boards like VPIC and BERS have a responsibility every 5 years? What was that responsibility?

Barry Bryant: That is the asset allocation study, to be completed every five years

Bob Rusten: Do you think, as our advisor, Burlington could address some of the structural problems we face in our retirement system through changes in our investment strategy?

Barry Bryant: I could have gotten you better returns the last six years. I could get you better returns the next five. But, improvements in investment approach will not be able to address the fundamental problems of your system – I can top off the rain barrel, but I can't fill it.

Mayor Weinberger: On average, we've done about a percent or two worse each of these years you are talking about – that's something substantial in a large fund. That's about \$9 million.

Barry Bryant: Agree, that's about \$9 million.

Councilor Knodell: [Barry] you have said you expect a rise in interest rates. A rise in interest looks certain to occur. How is VPIC positioned for that new environment?

Barry Bryant: They are better positioned for that environment higher interest rate environment

Joe Keenan: [Barry] if we aren't in a position to maximize our investment returns, we are not doing everything we can to improve the situation our retirement system faces. VPIC has a conservative approach that makes it unlikely we are going to achieve the 8 percent actuarial assumption.

Barry Bryant: Agree with everything you said. With respect to actuarial assumptions: Most (?) are projecting between a 5 and 7.5 percent return. This actuarial assumption should be thought of as a budgeting tool. Burlington has 90-odd percent of its assets invested in VPIC, and should probably use VPIC's actuarial assumption. But note - does everyone understand the impact of lowering the investment return actuarial assumption? Lowering the investment return projection will mean you need to increase the required tax contribution.

Barry Bryant, continued: (Reviews Dahab's portion of the City funds, which began split 90-10 between Dahab and VPIC; Dahab's returns have reduced that portion to 7 percent) I advocated for 5 - 5 timber and private equity. We have allocated 4 percent to timber and private equity and 2 percent in emerging markets - timber and emerging equity have underperformed relative to possible alternatives. Timber is doing better, and emerging markets have done poorly.

Mayor Weinberger: Your recommendation is to take money out of VPIC and run an alternative?

Barry Bryant: No - have BERS run model and then make a recommendation about whether to stay with VPIC.

Mayor Weinberger: How is the current 90/10 arrangement not an alternative?

Barry Bryant: Because the 10 percent is a supplement to VPIC, not an alternative.

Mayor: If you were to pursue a strategy that was at the 50<sup>th</sup> percentile - i.e., owning a little of everything to track market performance on average, could you come in with a lower set of fees - .02 vice .04 percent?

Barry Bryant: It is a little more complicated, but yes. I should add with VPIC you do have relatively low fees for the complicated type of investments you have.

Councilor Paul: I would also note that we are able to take advantage of economies of scale with VPIC

Jeffrey Wimette: Why did Dahab receive 10 percent of the initial allocation.

Councilor Bushor: It was a component of the deal to shift asset allocation at the time - necessary for making the deal.

Barry Bryant: I would close by saying, anything you need or questions you have - please just ask and let me know.

~ 6:00pm      **Discuss Whether Committee Wants to Pursue More Info on Investment Issues**

Bob Rusten: What do we as a Committee want to do further with respect to asset management and whether it can address the problems of our retirement system?

Councilor Bushor: Could a consultant help with this?

Bob Rusten: Barry and VPIC are technically consultants to the City

Councilor Paul: And VPIC has a consultant, as well – that's a number of consultants and fees that we may want to consider.

Councilor Knodell: VPIC came and did a presentation – do they seem inclined to make changes without increasing substantial risk? If so, maybe I'd consider leaving things where they are.

Councilor Paul: VPIC's 2013 performance was not good. They are interested primarily in preservation of capital, which means there is a conservative approach and will result in lower return in good years.

Eileen Blackwood: VPIC is conservative, and their expectation is lower than the actuarial assumption of an expected return.

Bob Rusten: I ask again, what do we as a Committee want to do further with respect to asset management and whether it can address the problems of our retirement system?

Councilor Mason: Recommendations to BERS to analyze asset allocation are appropriate, but it is not the purview of this Committee to try and manage asset allocation

Councilor Knodell: Chasing investment returns is not a good approach – we need to align our actuarial assumptions with our investment approach. We need alignment of the fundamentals to keep the system healthy.

Bob Rusten: What I am hearing thus far is: No more time on asset management, and not necessarily one of the ways to address our problem – is that fair?

Jim Strouse: It is a big deal. I agree that it [investment policy] is not going to solve the problem, but it will help address the underlying problem.

Joe Keenan: We have 4 or 5 bleeders to deal with [*in the retirement system*], but not a shot to the heart – we can't be complacent – doesn't mean we need

Jim Strouse: I am concerned by the Barry's note about PIMCO's analysis of VPIC's current portfolio and how it would have performed in a downturn.

Mayor Weinberger: We could take the passive approach (median return, lower cost) potentially as much as \$12 million better off – the \$9 million discussed earlier and ~\$500,000 a year in fees. That's an important component to consider as part of any solution. There is an argument to be made about minimizing expenses and owning the median.

Jim Strouse: I agree, though I would term it the market return – not the median return.

Councilor Bushor: How do you own the median return? And why is that a secure investment?

Mayor Weinberger: You invest in an index fund that purchases a reflection of the market.

Councilor Paul: You can invest in an index that tracks the market as a whole or a specific component of the market.

Bob Rusten: So I'm hearing four things:

- Potentially changing asset management
- Ask BERS to do more investigation
- Even if we thought we could improve return, wouldn't solve the underlying problem
- We should focus on other issues as well

Bob Rusten, continued: BERS has the authority to review this – not something we'd continue to look at, but something of interest

Mayor Weinberger: I think we should be specific and ask BERS to evaluate a low-cost median or market model, give it serious consideration.

Jim Strouse: Barry had specific recommendations on page 10 of Dahab's report

Chip Mason: Looking forward or backward? (answered: forward)

Councilor Knodell: Looking at ideal asset allocation model?

Bob Rusten: And identifying risk strategy as well. [*Directing BERS to do the analysis and identify the risk strategy*].

Mayor Weinberger: I would volunteer to write up the idea of the low cost median / market model and flesh out at next meeting

(Committee agreement to review the Mayor's proposal at the next meeting)

Joe Keenan: Agree, but would point out there is some urgency here to make a decision, because we are leaving money on the table with a poor return that does not make the assumed investment benchmark.

~6:30pm      **Review of Experience Study (FY13 Valuation Report)**  
                                  *Karen Paul*

Bob Rusten: So we will put that on the next agenda, and turn now to a discussion of actuarial assumptions (other than the investment return), with Councilor Paul giving us an overview.

Councilor Paul: The experience study is the foundation on which the City plans its funding needs, building assumptions about future estimates based on actual experience and trend projections. Our experience study showed that we are within our assumptions, but the investment returns do not hit the benchmark of 8 percent until after the 20 year window. Some highlights:

- More men and women are leaving before retirement age than expected, leading the City's actuary to propose some modest changes
- Most interesting is that from July 1, 2007 to June 30 2012 – noticeable stall in retirement because of bad economy
- Post-retirement mortality: slightly higher than expected for Class B, lower for Class A
- 3 percent inflation, 3 percent annual adjustment for those receiving full COLA
- Salaries and promotions figures have tracked the projections based on the experience study
- Investment return projected to be 6.59 percent for 10 years, 7.74 percent for 20 years, and 8.44 percent for 30 years

~6:40      **Discuss What Actuarial Assumptions We Need to Better Understand,**

## **Additional Data We Need, and How We Want To Proceed**

*All*

Bob Rusten: Other actuarial assumptions we have had interest expressed in include an open and closed system, open or closed amortization, and projected unit credit system. Anything else?

Jim Strouse: This is not an actuarial assumption, but a funding question. We do need to look more at how the system is funded – that's an important conversation.

Councilor Bushor: We should look at the open and closed amortization system.

Councilor Paul: Agree. Beth Pearce spoke about this issue in combination with another factor as potentially problematic.

Brian Lowe: The combination of the projected unit credit and the open amortization system.

Mike Flora: Does this affect the contribution or the unfunded liability?

Joe Keenan: Moving from a projected unit credit method to entry age normal, closed group/open group, open amortization are components we should ask the actuary to evaluate to see what the impact is on the system.

Mayor Weinberger: We work from the current expected lifespan, and don't adjust for changes in the experience study – when we are looking out thirty years in the future, we need to account for demographic change. This is potentially an issue that understates the risk to the system. We ought to discuss this particular component as well.

Jim Strouse: We should bring David Driscoll back to discuss the different funding methods [*those described by Joe Keenan*]. Let's look at that and see what the real effect is, and what the savings or costs could be. Maybe time to look at some change.

Mike Flora: Jim, when you talk about funding methods, are you also looking at the pension structure itself?

Jim Strouse: No. Only the methods.

Bob Rusten: So ask Buck to come in and talk about these funding methods provided they are actuarially sound. (by sound, Bob clarifies, increase funding level and decrease the contribution level)

Jim Strouse: Yes. What kind of funding methods could help us address the problem we're in.

Bob Rusten: The goal of this committee is the issue with the retirement system. So, if Buck runs these numbers and saves \$100 it hasn't addressed the issue the committee is charged to address

Jane Knodell: Bob, it is not just about the funding level and contribution level, but also a question of building a sustainable committee.

Bob Rusten: Agree. Jim, would you be willing to help fund this?

Jim Strouse: This is a City Council committee.

Chip Mason: Could we put the questions to Buck and David Driscoll in writing, and make it more affordable?

Jim Strouse: On board for that.

Eileen Blackwood: Or do it on the phone.

Jim Strouse: Can you call David and see what the cost would be?

Bob Rusten: I will do it, but with agreement of the committee, I'd like to arrange to get the answers from David if they are affordable and I'll use my best judgement about what affordable is.

(Committee agrees)

Bob Rusten: We are out of time and we have committed to keep these meetings on schedule. I will close with what we have agreed for the next agenda

- Mayor's proposal
- Buck Response
- Goals and Process for Consultant Selection
- Timeline and work plan
- GASB 68

Jim Strouse and Bob Hooper: What about waiting to the 15<sup>th</sup> for the next meeting?

Bob Rusten: Three people cannot meet on the 15<sup>th</sup>. We will plan to keep it on the 8<sup>th</sup>, with Jim and Bob hoping to call in.

Next Meeting Time: **Tuesday, April 8, 2014 5pm – 7pm** (Location TBD)

**Topics for Future Agendas:**

- Presentation by John Federico and Bob Rusten on the 20 year history of the system
- GASB 68